ORIGINAL

COLE, RAYWID & BRAVERMAN, L.L.P.

ATTORNEYS AT LAW
SECOND FLOOR
1919 PENNSYLVANIA AVENUE, N.W.
WASHINGTON, D.C. 20006-3458
(202) 659-9750

JOHN P. COLE, JR.
BURT A. BRAVERMAN
ROBERT L. JAMES
JOHN D. SEIVER
WESLEY R. HEPPLER
PAUL GLIST
DAVID M. SILVERMAN
JAMES F. IRELAND, III
STEVEN J. HORVITZ
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ANN FLOWERS
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SUSAN WHELAN WESTFALL
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SANDRA GREINER
JAMES W. TOMLINSON
MARK S. KRISTIANSEN
CHRISTIN S. MCMELEY+
HEATHER M. WILSON
DAVID N. TOBENKIN*

+ADMITTED IN OKLAHOMA ONLY
*ADMITTED IN CALIFORNIA ONLY

ALAN RAYWID
(1930-1991)

OF COUNSEL
FRANCES J. CHETWYND
ELLEN S. DEUTSCH

FACSIMILE
(202) 452-0067

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Hand Delivered
Ms. Magalie Roman Salas
Office of the Secretary
Federal Communications Commission
445 Twelfth Street, S.W.
Room TW-A325
Washington, D.C. 20554

Re: Inter-Carrier Compensation for ISP-Bound Traffic
CC Docket No. 99-68

Dear Secretary Salas:

Enclosed please find an original and four (4) copies of the Reply Comments of Global NAPs Inc. in the above-referenced proceeding. The attached document was also filed electronically via the ECFS system.

Please return a filed-stamped copy of this letter to me in the enclosed stamped, self-addressed envelope.

Very truly yours,

Christopher W. Savage

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Before The
Federal Communications Commission
Washington, D.C. 20554

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In the Matter of Implementation Of The Local Competition Provisions in the Telecommunications Act of 1996 Inter-Carrier Compensation for ISP-Bound Traffic	CC Docket No. 96-98 CC Docket No. 99-68

REPLY COMMENTS OF GLOBAL NAPS, INC.

GLOBAL NAPS, INC.

Christopher W. Savage
Karlyn D. Stanley
COLE, RAYWID & BRAVERMAN, L.L.P.
1919 Pennsylvania Avenue, N.W., Suite 200
Washington, D.C. 20006
202-659-9750

William J. Rooney, Jr
General Counsel, Global NAPs Inc.
Ten Merrymount Road
Quincy, MA 02169
617-507-5111

Date: April 27, 1999

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Before The
Federal Communications Commission
Washington, D.C. 20554

In the Matter of Implementation Of The Local Competition Provisions in the Telecommunications Act of 1996 Inter-Carrier Compensation for ISP-Bound Traffic	CC Docket No. 96-98 CC Docket No. 99-68

REPLY COMMENTS OF GLOBAL NAPS, INC.

1. Introduction and Summary.

The comments in this matter break down along predictable lines. ILECs continue their assault on paying any compensation for ISP-bound traffic at all, relying on a combination of flawed legal reasoning and economic legerdemain. CLECs, who incur the costs that the ILECs do not want to pay, explain why compensation makes sense and is perfectly legal.

Global NAPs, not surprisingly, is in the CLEC camp. Even as it expands into other market segments, Global NAPs is making a successful business out of meeting ISPs' burgeoning need for connections to the public switched network. Because a large portion of the costs involved in this business are costs caused by the ILECs' end users — who call ISPs that Global NAPs serves — Global NAPs has a keen interest in the legal and regulatory regime governing inter-carrier compensation for such traffic. By the same token, having focused its market entry efforts on the needs of ISPs, Global NAPs has some perspectives on this market segment that the ILECs, and even many CLECs, do not.

The comments make clear that the ILECs remain in a state of total denial regarding the competitive and economic realities affecting ISP-bound traffic. These realities can be briefly summarized. When a CLEC provides ISPs with connections to the public switched network, it incurs certain costs that are caused by the ISPs. These are the costs of the ISPs' loops (*e.g.*, ISDN PRI lines) and associated switch port costs. These costs should be recovered from the ISPs. The CLEC also incurs costs when an ILEC's end users call ISPs served by a CLEC. These are primarily the costs of switching the incoming traffic to the proper ISP loop. Logically, these costs should be recovered from the cost causers, *i.e.*, the ILEC's end users; but because the CLEC has no direct relationship with those end users, cost recovery must come from the ILEC.

The situation is parallel for the ILEC. When an ILEC provides ISPs with connections to the public switched network, it too incurs costs that are caused by the ISPs — the cost of the loops and switch ports used to serve them. And when the ILEC's customers call an ISP, they cause the ILEC to incur additional, usage-related costs. These include the cost of switching the calls at the originating switch, the cost of transporting the calls to the switch that serves the ISP, and the cost of switching the calls on to the proper ISP loop. ***These*** costs, including terminating switching costs, should be recovered from the end users making the calls and thereby causing the costs to be incurred. But whether these costs are fully recovered from end users or not, the ILEC incurs them when it serves the ISP. Moreover — and critical here — the ILEC avoids some of them when a CLEC serves the ISP instead.

So: the ILECs' customers cause the costs incurred by CLECs when they switch incoming calls to ISPs; and the ILEC avoids these costs when a CLEC performs that function. In these circumstances, it makes no sense to assert that ILECs should be able to deliver calls to CLECs for routing to an ISP, and then pay the CLEC ***nothing at all*** for the work that the CLEC does or, alternatively, for the costs that the CLEC allows the ILEC to avoid. To the contrary, the economically most rational and efficient regime would be one in which the CLEC would be assured of getting paid at least what it would cost the ILEC to perform the same functions; this would provide sound economic signals to potential entrants to undertake this function if they can do it more efficiently than the ILEC can, and to avoid it if they cannot.

The ILECs make some half-hearted attempts to justify their "no pay" proposal in economic and competitive terms, but these are plainly unavailing. The real ILEC thrust in this regard is an effort to generate legal and regulatory confusion. But in fact the matter is fairly simple. The Commission may treat ISP-bound traffic as a species of interstate traffic subject to Section 201(a) of the Act, and establish a rational regime for inter-carrier compensation under that authority. Or it may exercise its authority under Section 201(b) of the Act — affirmed by the Supreme Court in *AT&T v. Iowa Utilities Board* — and establish regulations under Section 251 and Section 252 which would require ISP-bound traffic to be treated like local traffic under Section 251(b)(5). The Commission can reach any substantive result that makes policy sense under either legal theory.

The Commission's choice of legal theory will determine the role of Section 252(i). To the extent that compensation obligations are based on Section 251(b)(5), then Section 252(i) applies. This is the case today where state commissions have ruled that ILEC interconnection agreements embrace ISP-bound calls. ***How*** Section 252(i) applies to particular provisions of particular contracts is a matter that the Commission has, in the first instance, left to the states. There is no reason to modify that situation here. In this regard, ILEC fears of "daisy chaining" of agreements are, and always have been, illusory. In any event, if future compensation obligations are based directly on Section 201, then Section 252(i) does not apply.

Finally, Global NAPs must take issue with those who assert that dial-up traffic from end users to ISPs is not reasonably severable into interstate and intrastate components. It is probably true that perfect accuracy in this area is not possible. That said, it is reasonable to conclude that more than 90% of the actual traffic traversing the ILECs' and CLECs' facilities en route to the ISP is entirely and unambiguously "local" in nature. This is true for the simple reason that for the vast majority of the time that most end users are on line, the only signals being sent begin and end at the end user's modem and the ISP's modem. These signals ***never*** travel to any distant "Internet sites" at all. Just as Feature Group A lines were subject to reasonably estimated "percent interstate use" factors, ISP-bound calls could reasonably be estimated as about 90% intrastate (and local) and about 10% interstate.

2. Compensation For ISP-Bound Calls Is Economically Reasonable, Irrespective Of Whether The ILEC Is Fully Recovering Its Costs From Its Customers.

a. ILECs Can Run, But They Cannot Hide From The Costs Their Customers Cause.

A CLEC incurs substantial costs (mainly, but not exclusively, switching costs) when it delivers calls originated by another LEC's customers to an ISP. Despite these costs, the ILECs complain that it is unfair and unreasonable to expect them to pay the CLECs when the CLECs do this work on behalf of the ILECs' customers. These ILEC complaints are unfounded.

Ameritech argues that it should not have to pay because it loses money when its customers call ISPs (whether the ISPs are served by a CLEC or not).[1] Global NAPs seriously doubts that Ameritech or any other ILEC actually loses money from its local exchange services, including those services provided to customers who call ISPs.[2] But even if the ILEC is losing money, the CLEC should still be paid, because the CLEC's efforts allow the ILEC to avoid significant costs that the ILEC itself would otherwise have to incur.

Consider what would actually happen in a regime where the ILEC did not have to pay when its customers call ISPs served by a CLEC. Any CLEC that wanted to stay in the business of serving ISPs would have to establish a pricing structure in which the ISP paid for the costs of incoming calls, including, in particular, the costs of switching such calls to the proper ISP loop. In light of the long-standing ISP access charge exemption, no ISP would find it economically feasible to obtain service from such a CLEC. Instead, the ILEC's services (business line services tariffed at intrastate rates) would necessarily be substantially less expensive. It follows that if a CLEC is forced to recover from ISPs the costs caused by ILEC customers calling those ISPs, the CLEC would soon have no ISPs as customers. The ISPs, in

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[1] *See* Ameritech Comments at 3-10 and Attachment A.

[2] The last time the RBOCs tried to claim they were losing money on ISP-bound calls, the Commission rejected that claim. *See Access Charge Reform*, 12 FCC Rcd 15982 (1997) at ¶ 346, *affirmed sub nom. Southwestern Bell v. FCC*, 158 F.3d 523 (8th Cir. 1998).

turn, would find that the only source of dial-in connections to the public switched network available to them on reasonable terms was the ILEC.

Put aside for a moment the anticompetitive aspects of this situation. From a cost perspective, this shows that in the long run ***the ILEC cannot escape bearing the costs its customers cause by calling ISPs.*** Any CLEC to whom it effectively "exports" those costs will not be able to compete in the market for the business of ISPs. The ISPs served by such a CLEC will migrate to other suppliers — either to a CLEC that ***is*** being paid by the ILEC, or back to the ILEC itself. Either way, the costs return to the LEC serving the cost causer — the ILEC serving the customers calling the ISP.

For these reasons, the precise amount of revenues that the ILEC receives from its customers is economically irrelevant to the need for, or proper level of, inter-carrier compensation. When a CLEC serves an ISP that receives calls from the ILEC's customers, the ILEC avoids the costs that ***it*** would otherwise incur if it had to deliver the calls to the ISP using its own facilities. If the ILEC avoids these costs without paying the CLEC, its bottom line is increased by the amount of the avoided cost. On the other hand, if the ILEC is required to pay the CLEC for the CLEC's efforts in completing these calls, the ILEC is no worse off than if the ILEC did so using its own facilities.

All of these results flow directly from the ISP access charge exemption, which is sound public policy and which the Commission has expressly taken "off the table" in this proceeding.[3] This is the so-called "modem tax." If ISPs paid per-minute access charges to the LEC providing their dial-in connections to the public network, those payments would compensate that LEC for the switching costs associated with calls that are incoming to the ISP (and the costs of the originating LEC besides). Under this scenario, just as long distance carriers bill their

[3] *See* In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Inter-Carrier Compensation for ISP-Bound Traffic, *Declaratory Ruling in CC Docket No. 96-98 and Notice of Proposed Rulemaking in CC Docket No. 99-68,* CC Docket Nos. 96-98 and 99-68 (released February 26, 1999) ("*Notice*") at ¶ 34.

customers usage-sensitive rates high enough to cover access charges along with other costs, so too ISPs would be forced by economic necessity to move to usage-sensitive pricing.

But as the Commission is well aware, in economic terms calls to ISPs are treated like local calls, which are handled on a "sent paid" basis. Under this regime — the one actually in place — the money to cover the cost of an end user calling an ISP comes from (or should come from) the end user, not the ISP. Under ***this*** scenario, there is no question that the originating LEC has to pay the terminating LEC for the costs generated by the end users of the originating LEC. No amount of jurisdictional musings or economic legerdemain can change this stubborn economic fact.[4]

b. Compensation For ISP-Bound Calls Does Not Distort Competition.

The discussion above assumes that the ILEC is not paying the CLEC more than the ILEC's cost of terminating calls to ISPs. This assumption is obviously false in the case of some interconnection contracts. From this perspective, much of the controversy surrounding this issue has arisen because of some severe errors in ILEC business judgment in negotiating and/or litigating reciprocal compensation rates. Basically, ILECs thought that their position as incumbent monopolists assured that they would be net receivers of calls, so they pressed for the highest compensation rates they could remotely justify. They ended up with rates in many interconnection agreements that far exceed both their costs and, probably, the costs of many

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[4] For this reason the suggestion that the proper result in this matter is for CLECs to share their "access" revenue from ISPs with ILECs — while clever — is unadulterated economic nonsense. *See, e.g.,* US West Comments at 10-11; BellSouth Comments at 8-9.

CLECs as well.[5] To the extent that holding ILECs to the consequences of such business errors is a problem, it will tend to correct itself over time.[6]

For this reason, Southwestern Bell and other ILECs are completely misguided in their claims that paying CLECs compensation for delivering calls to ISPs distorts the competitive process in any way.[7] Any distortion in CLEC incentives to serve ISPs as compared to other market segments arises entirely by virtue of the bad ILEC business judgment described above. ILECs should not be surprised that when they demand enormously high rates (compared to their cost) for terminating calls on their networks, CLECs — entitled to receive the same amount by virtue of the Commission's rule requiring symmetrical compensation — respond by targeting their marketing efforts on customers who receive calls, rather than make them.

In this regard, it is breathtakingly hypocritical for the ILECs to claim that ***CLEC*** activity is slowing the growth of local exchange competition. It is now more than three years since every ILEC in the country has had an affirmative duty under Section 251(b) and Section 251(c) to open up its local exchange and exchange access markets to competition. In the case of the RBOCs, the Section 271 process constitutes a kind of public scorecard with regard to how well they are fulfilling those duties. The results posted on that scorecard are clear: despite the fact that there are RBOC-owned local carriers in almost 50 states, ***not one RBOC has obtained Section 271 certification for any state,*** and there have only been a handful of applications. The RBOCs have plainly made the business decision that, on the whole, keeping

[5] Several factors would support a conclusion that a CLEC will have much higher costs than an ILEC in performing otherwise similar functions. These include the fact that the CLEC will almost certainly lack economies of scale and will face enormously higher capital costs (both in terms of access to funds and in terms of a competitively appropriate depreciation life for the relevant equipment) than will the ILEC. CLECs may be able to overcome some of these plain cost disadvantages in some cases by means of specialization and the deployment of only the newest, most efficient technology, but there is no *a priori* reason to think that even these efforts will result in costs below those of the ILEC. In any case, as described below, it makes neither economic nor regulatory sense to focus on CLEC costs at all.

[6] *See* Section 5, below.

[7] *See, e.g.,* Southwestern Bell Comments at 19-21; Bell Atlantic Comments at 1, 3-4.

a stranglehold on their local monopolies is worth more to them financially than losing their monopolies and getting into the long distance business.[8] ***That*** is the source of the slow development of local competition, not the efforts of CLECs to find niches where they can make inroads despite the ILECs' efforts to squelch them.[9]

Any doubt about this situation can be dispelled by reviewing Bell Atlantic's recent Section 271 filing in New York. Knowing that its Section 271 filing would be pending, Bell Atlantic-New York — unlike many other Bell Atlantic subsidiaries — is actually paying compensation for ISP-bound calls in accordance with the directives of the New York PSC. In its application, Bell Atlantic is quick to try to defuse this issue: "Neither the FCC's ruling nor the ongoing proceedings before [the New York] Commission affect the way that BA-NY does business today. BA-NY is continuing, under protest, to pay reciprocal compensation consistent with current [New York] Commission rulings, unless and until those rulings are modified."[10] In other words: when its ***actual compliance*** with its Section 251 duties, as embodied in Section 271's checklist, is at issue, Bell Atlantic pays. Bell Atlantic's behavior on this topic in other jurisdictions must be evaluated in this light.

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[8] In raw economic terms, that may be a perfectly rational business decision. As long distance service becomes ever-more competitive, an RBOC could quite reasonably conclude that it would rather hold onto its monopoly than trade it away for the uncertain financial rewards of offering interstate calling for 5¢ per minute, with Sunday calling free.

[9] The ILECs would apparently have the Commission believe that factors such as enormous price and non-price barriers to efficient collocation arrangements; extensive litigation over unbundled loop prices; a variety of anticompetitive practices regarding access to premises wiring in apartment buildings and offices; and extensive delays in making electronic access to operations and support systems available to competitors, are all minor, inconsequential issues that have little to do with the pace of competition. The Commission should also note that few if any states have established competitively neutral universal service funding mechanisms that would allow non-incumbents to obtain the same subsidies for providing residential local service that the ILEC itself enjoys, further complicating the process of competitive entry to serve the broad market.

[10] Petition of New York Telephone Company for Approval of its Statement of General Available Terms and Conditions Pursuant to Section 252 of the Telecommunications Act of 1996; and Draft Filing of Petition for InterLATA Entry Pursuant to Section 271 of the Telecommunications Act of 1996 to provide In-Region, InterLATA Services in the State of New York, *Joint Supplemental Affidavit of Donald E. Albert, Julie A. Canny, George S. Dowell, Karen McGuire and Patrick J. Stevens on Behalf of Bell Atlantic - New York* (Case No. 97-C-0271, filed April 13, 1999) at 106-07.

From Global NAPs' perspective, much of the ILECs' enormous intransigence on this question arises from their intense desire not to be placed in the vise of actually having to ***pay*** someone else the same rate, for the same function, that the ILEC wants to ***charge*** everyone else. This desire underlies the ILECs' claim that there are some special efficiencies that CLECs experience in routing traffic to ISPs that the ILECs themselves do not experience when they perform a generic minute of local switching. The Commission should see this effort for what it is — an ILEC effort to avoid the true market impact of rates that the ILEC itself claims to be reasonable.

In addition to serving this ill-motivated regulatory purpose, these ILEC arguments suffer from a key economic flaw as well. The "default" provider of connections between ISPs and the public switched network is the ILEC. It costs the ILEC some amount of money, in real economic terms, to route calls to ISPs. The Commission has stated that it wants to establish rules that encourage the efficient entry of new competitors.[11] In this context, that means that the price signal to which the new entities should be responding is a price that equals ***the ILEC's own costs***. With that pricing regime in place, new entrants who are more efficient than the ILEC will have an incentive to enter the market, while those who are not, will not. And those new entrants who are most efficient at performing that function (through whatever technology is appropriate at any particular time) will have the greatest competitive advantage in seeking to obtain ISP customers, both from the ILEC and from other CLECs.

The Commission should be ***encouraging*** the use of these new, efficient technologies. For this reason, the Commission should staunchly resist any temptation to require that compensation for handling ISP-bound traffic to be based on CLEC-specific costs. That is a bad idea for the same reason that price cap regulation is superior to rate of return regulation. Indeed, the best way to understand the workings of a regime that ties CLEC compensation to an independently established ***ILEC*** price (whether local call termination under Section 251(b)(5) or

[11] *Notice* at ¶ 33.

interstate local switching under Section 201) is precisely as a "price cap" regime, with the CLEC's "price cap" determined by the ILEC's price.[12]

c. ILEC Fears Of Reforming Pricing For Local Calling Have No Proper Bearing On This Proceeding.

Historically, ILEC retail prices for incremental usage of the network have been either too high or too low. If, as the ILECs note, the average non-Internet call has a duration of three minutes, then the actual cost to the ILEC of handling a "voice" call is certainly no more than \$0.012, and probably less.[13] But customers on service plans that measure local usage typically have message unit charges far about that level.[14] On the other hand, while flat-rated local calling plans typically have a "usage allowance" — indeed, often a substantial allowance — built into the price, the actual incremental revenue the ILEC receives for each call is zero.

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[12] In the abstract, such a regime creates an incentive to establish a compensation rate that is, indeed, a "reasonable approximation of the additional costs" of terminating calls, as contemplated by Section 252(d)(2) of the Act. Bell Atlantic recognized as much in a rare moment of candor in its reply comments on reciprocal compensation in May 1996. Dismissing fears of CLECs and others that ***any*** compensation regime other than bill-and-keep would be an open invitation to abusive ILEC overpricing, Bell Atlantic explained that if the ILECs overpriced interconnection, they would be immediately punished in the market by CLECs who focused on serving customers who primarily receive calls — including, specifically, ISPs:

> [T]he notion that bill and keep is necessary to prevent LECs from demanding too high a rate reflects a fundamental misunderstanding of the market. If these rates are set too high, the result will be that new entrants, who are in a much better position to selectively market their services, ***will sign up customers whose calls are predominantly inbound,*** such as credit card authorization centers and ***internet access providers.*** The LEC would find itself writing large monthly checks to the new entrant.

Reply Comments of Bell Atlantic, CC Docket No. 96-98 (filed May 30, 1996). Of course, this is how things actually turned out.

[13] If end office switching has a cost of (say) \$0.002/minute, three minutes of switching costs \$0.006. Assuming that two end offices are involved in 66% of calls, that adds another \$0.004. An allowance of \$0.002 for any necessary tandem switching and interswitch transport is, if anything, generous.

[14] For example, Ameritech's residence message unit in Wisconsin is 5¢ per call, and its business message unit is 10¢ per call. *See* Ameritech Comments, Attachment A.

From this perspective, the pro-competitive reciprocal compensation provisions of the 1996 Act are having exactly the impact that one would expect: they create pressure on economically irrational pricing regimes — including local service pricing regimes — developed for a monopoly era. This proceeding is not the place to explore and debate what might constitute a rational and competitively sustainable pricing regime for local calling. However, the fact that ILECs are complaining about the impact of reciprocal compensation for ISP-bound calls on their local exchange costs and revenues is not an indication that there is a problem to be solved. To the contrary, it is an indication that the 1996 Act is working as it was intended to do.[15]

For this reason, it would be a serious mistake for the Commission to use LEC complaints about pressures on their local calling plans and rates as a basis for deciding any aspect of this proceeding. The only way in which a cost-based reciprocal compensation regime would ***not*** put pressure on an ILEC local calling plan is if that plan were already economically sensible and appropriate for a competitive market. Again, the existence of such pressure shows that the law, as currently being implemented, is working, not that it is flawed.

In economic terms, this is probably the reason that ILECs are eager to get ISP-bound calls classified as something ***other than*** local calls. If ISP-bound calls are treated as local,

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[15] The problem of rationalizing local calling pricing is far from insurmountable. Suppose that the average incremental end-to-end cost of a local call is $0.004/minute. LECs could establish local calling plans that reflect that cost based on overall average local usage by their customers. If the average customer spends 20 hours on the telephone per month, for example, the local calling plan should be priced at the cost of the loop, plus $4.80 (20 hours x 60 minutes = 1200 minutes, x $0.004/minute = $4.80). (If the loop itself is viewed as too expensive, that, of course, should be addressed by means of competitively neutral universal service arrangements under Section 254.) In this regard, it is quite likely that traditional state-level antipathy towards "measured-" or "message-rated" local service plans arises from ILEC overpricing of usage. Again, assuming an end-to-end local calling cost of $0.004/minute, even the 39 hours of monthly ISP-bound calling Ameritech postulates would cost only $9.36 per month, beyond the cost of the loop (39 hours x 60 minutes = 2340 minutes x $0.004/minute = $9.36). If it is further assumed that high-usage lines reflect only a fraction (say, one-half) of the total, then overall average usage per line would be 1770 minutes per month, for a usage cost of $7.08. Rationalizing local calling plans throughout the nation will obviously be a complex and politically charged process. But once it is recognized that usage costs ***including Internet usage*** probably only average $5.00 to $10.00 per customer per month, it is clear that the problem is not even remotely insurmountable.

then the dramatic increase in calls to ISPs is a sign that existing local calling plans may be "broken" and in need of reconsideration by ILECs and state regulators. But if ISP-bound calls can be removed from the mix of normal local calls, it may be that the day of competitive reckoning for existing local calling plans may be deferred. There is no reason, however, for the Commission to facilitate this deferral.[16]

3. Commission-Established Parameters For Negotiations Are Needed To Break The Current Logjam On This Issue.

If, as explained above, the ILECs avoid significant costs when CLECs serve ISPs, why aren't the ILECs be lining up to pay CLECs to do so? Presumably the parties could agree on a rate for handling such calls that is higher than zero but less than or equal to the ILEC's avoided cost. Indeed, if a CLEC can actually deliver calls to ISPs at a cost that is lower than the ILECs' avoided cost, then overall economic efficiency would be served by encouraging CLECs to undertake this role.

In the abstract, and writing on a completely clean slate, parties should logically be able to reach such economically efficient arrangements. But in the real world, several factors eliminate any meaningful possibility of such deals actually being cut now, without clear regulatory guidelines from the Commission. As a result, as discussed below, while Global NAPs supports the Commission's proposal to rely on negotiations to resolve these issues, Commission guidance on the parameters of such negotiations is necessary.

[16] To the contrary. If local exchange service is underpriced by virtue of legacy monopoly pricing arrangements, that in itself will be a substantial barrier to local exchange competition, since new entrants would be competing against a subsidized service — a daunting proposition, to say the least. To the extent that a state wants to keep local exchange service underpriced, the state must act under Section 254 to establish a competitively neutral funding regime under which new entrants can obtain the same subsidies that the ILEC obtains in providing such services. Banning or limiting compensation for ISP-bound calling hardly constitutes a pro-competitive, competitively neutral response to this situation.

The ILECs' monopoly mindset hampers negotiations. One reason clear Commission guidance is needed is the ILECs' historical monopoly mindset. It is simply not in the cards for an ILEC to acknowledge that it cannot serve any customer group — even a disfavored group like ISPs — in an efficient manner compared to other carriers. While abstract economic logic would dictate that ILECs should be grateful to CLECs who take the task of serving ISPs off the ILECs' hands, the practical realities of corporate culture make such gratitude hard to come by.

In this regard, ILECs have undoubted economies of scale and CLECs do not. One of the few ways that small CLECs can hope to compete against the ILECs is by countering economies of scale with *economies of specialization.* A Global NAPs or a Focal Communications or a COVAD will not be in a position, immediately after starting operations, to offer a full range of local exchange and exchange access services to a full range of customers. Just as MCI started out as a provider of microwave-delivered interstate private lines and MFS started out as a provider of fiber-delivered special access circuits, today's new competitors — if they are to survive — need to identify "niche" markets where ILEC inattention, poor service, or monopoly-era pricing anomalies create business opportunities. The Commission should encourage this process to the maximum extent possible. It is the only way to use economic and market forces, as opposed to raw regulatory fiat, to force the ILECs to open their local markets to competition.

The ILECs have entrenched positions on the issue of compensation for ISP-bound calls. The Commission must recognize that at this point it is not writing on a remotely clean slate. We are now more than three years into the implementation of the 1996 Act, and a regime has developed under which the "standard" answer is that ILECs must pay compensation for ISP-bound calls.[17] The ILECs are suffering under this regime as a result of their own bad business

[17] As Focal Communications points out, prior to the Commission's *Declaratory Ruling*, every state commission to consider the issue concluded that calls to ISPs were subject to reciprocal compensation like any other local call. Focal Communications Comments at 2 n.6. Since the *Declaratory Ruling*, while one state (Missouri) has chosen to affirmatively "punt" on the issue until (continued...)

judgment in negotiating interconnection agreements.[18] The normal intra-corporate effort to avoid blame for such a blunder, however, precludes ILECs from acknowledging that ***they*** committed any errors at all; the error ***must be*** on the part of regulators who required compensation for such calls. This is not a mind-set conducive to open and efficient negotiations.

The ILECs can harm their competitors by dragging out negotiations and litigation. As the Commission is aware, the *status quo* for years has been that ISPs are treated like any other local business customers, able to receive local calls from other customers. This led to a situation in which ILECs and CLECs alike negotiated interconnection agreements under which calls to ISPs are subject to normal reciprocal compensation obligations.[19] Based on the view that reciprocal compensation obligations extended to ISP-bound calls, CLECs as a whole have rapidly expanded into this market segment. The result has been that a substantial part of the growth in the number of ISP connections to the public switched network have been provided by CLECs, not by ILECs.[20]

In these circumstances, to change ***now*** to a rule in which there is no compensation for ISP-bound calls, even for a period during which some sort of negotiations could occur, would simply disrupt CLEC cash flow and provide a completely unearned windfall to the ILECs. This is because (a) ILEC customers are not going to stop calling their ISPs and (b) it will take some

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[17](...continued)
this Commission concludes this rulemaking proceeding, all other state commissions to address the question — Florida, Alabama, Nevada, and Oregon (as well as an arbitrator in Delaware) — have concluded that such compensation should continue.

[18] Basically, as noted above, the ILECs assumed that their status as incumbent monopolists would lead to net incoming traffic, so they worked to establish high call termination rates.

[19] *See* Focal Communications Comments at 2 n.6.

[20] Global NAPs submitted information with its comments that shows that in the Boston LATA, Bell Atlantic serves less than one-third of ISPs, and is not even the largest supplier of ISP connections to the public switched network. CLECs in that LATA collectively serve well over half of the ISPs operating there.

time for the ISPs now served by CLECs to disconnect their service and reconnect with the ILECs (which would be their only economically rational choice, as described above).

For these reasons, nothing would serve the ILECs better than an "interim" arrangement in which no compensation is due until a new round of negotiations is completed (and, if necessary, arbitrated or litigated).[21] If CLECs reasonably believe that they will eventually get some reasonable level of compensation for ISP-bound calls, they will be reluctant to simply cease serving ISPs in the interim. But the longer the ILECs drag out the process, the longer the ILECs can keep the money their end users pay for delivering traffic to ISPs while at the same time avoiding the full costs of performing that service.[22]

The *ILECs' historical and competitive antipathy for ISPs will hinder meaningful negotiations.* An additional reason that compels the establishment of rules requiring compensation for ISP-bound calls is the ILECs' long-standing antipathy towards ISPs. Indeed, in discussing these questions it is common for ILECs to denigrate ISPs as somehow not being "real" or "legitimate" customers, and to denigrate the CLECs who serve them as somehow not being "real" or "legitimate" carriers.[23]

This reflects the fact that, as described in Global NAPs' original comments, ILECs do not like doing business with ISPs. This fact arises for a number of reasons. ISPs have specialized needs that ILECs are loathe to accommodate, such as efficient collocation and

[21] *See, e.g.,* GTE Comments at 19-20; Bell Atlantic Comments at 6.

[22] With hundreds of millions of dollars on the line, there is no end to the expected inventiveness of ILEC regulatory lawyers in creating seemingly plausible grounds for arguing that — no matter how sensible and logical compensation for ISP-bound traffic might ***seem*** (ILECs get paid by their customers to carry calls all the way to ISPs; CLECs who serve ISPs save the ILECs hundreds of millions of dollars in switching and related costs) — there is always "really" some reason that compensation should not be paid. For this reason, Global NAPs strongly urges the Commission to make absolutely clear in this proceeding that compensation must be paid to CLECs who deliver ILEC-originated traffic to ISPs (unless that right is affirmatively and expressly waived as a result of fair negotiations). Otherwise, the Commission can count on interminable litigation on this topic.

[23] *See, e.g.,* Bell Atlantic Comments at 3-4.

FX/number aggregation arrangements. ISPs depend heavily on their telecommunications arrangements, and at the same time tend to be technically sophisticated (often much more sophisticated than typical ILEC business office and repair personnel). As a result, ISPs can be very demanding customers. They want their service to work on a "24x7" basis, and when it doesn't, they want it fixed ***now.*** And when the ILEC's service is not up to par, ISPs as a group have no tolerance for ILEC efforts to shift the blame for service problems to the ISPs' or end users' customer premises equipment. This has led to a situation in which ILECs often view ISPs as burdens to be borne, not customers to be served.[24]

It is also no coincidence that the major ILECs all have their own ISP affiliates that compete with independent ISPs — the same independent ISPs that increasingly obtain their public switched network connections from CLECs. To the extent that ILECs are able to interfere with the business operations and viability of major suppliers to independent ISPs, the ILECs automatically provide aid and comfort to their own ISP affiliates. If the ILECs themselves had no "stake" in the ISP market as such, their efforts to cripple CLECs that serve independent ISPs — while misguided — might not be so plainly anticompetitive. Given the ILECs' interest in that market, however, it is impossible to view such efforts as in any sense legitimate or benign in motivation.

Commission rules are needed now in order to avoid endless regulatory gamesmanship by ILECs. The ILECs have every motivation to play "hide the ball" on this issue. Millions of dollars of cost and revenue are at stake. For this reason, the issue as they present it shifts over time, from the logic of bill-and-keep, to the scope of fee-based reciprocal

[24] It is ironic indeed that Bell Atlantic refers to "Internet discussion groups" as a source of evidence regarding any aspect of this controversy. *See* Bell Atlantic Comments at 3 n.3. Global NAPs questions the overall reliability of information obtained from "the Internet" as such. (The Commission, for example, will recall the wave of rumors surrounding the issuance of the *Declaratory Ruling* to the effect that the Commission was going to eliminate the ESP access charge exemption and re-establish the "modem tax.") But if comments on the Internet are relevant, one need only participate in discussion groups such as INET-ACCESS, CYBERTEL or USWEST-ISPLIST to learn of repeated ILEC bungling and technical incompetence — if not affirmative anticompetitive practices — in meeting ISPs' critical telecommunications needs.

compensation, to the adequacy of local calling rates, to universal service obligations and subsidies, to separations reform, to state-federal jurisdictional questions, and back again. For this reason, it is critical that the Commission keep its eye firmly on the economic reality here: the ILECs want to continue to charge their customers for calling ISPs; they want the CLECs to incur the costs the ILECs would otherwise incur in switching those calls to ISPs; and they want to keep the money from their end users, enjoy the cost savings, and pay the CLECs nothing.

4. The Commission May Lawfully Require Compensation For ISP-Bound Calls.

The Commission and affected parties have spent an enormous amount of intellectual capital on the question of state versus federal ***jurisdiction*** over ISP-bound calls. While that question is, indeed, complex, those complexities are largely irrelevant to the Commission's legally permissible options for establishing rules regarding compensation for such calls.

The Supreme Court in *AT&T v. Iowa Utilities Board* held that the Commission's general authority under Section 201(b) to issue regulations necessary to implement the entire Communications Act extends to the provisions of the Telecommunications Act of 1996 that are codified in the Communications Act itself — including Sections 251 and 252.[25] States that choose to handle mediations and arbitrations under the Act are bound by the rules that the Commission adopts.[26]

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[25] *AT&T v. Iowa Utilities Board,* ___ U.S. ___, 142 L.Ed. 834, 849 (1999) ("We think that the grant in § 201(b) means what it says: The FCC has rulemaking authority to carry out the "provisions of this Act," which include §§ 251 and 252, added by the Telecommunications Act of 1996") (footnote omitted).

[26] A state that chooses to undertake its responsibilities of Section 252 is bound to follow this Commission's rules implementing Sections 251 and 252. A state that chooses not to do so, whether out of disagreement with those rules, a perceived lack of state-level legal authority, or any other reason, is free to sit on its hands. In that case, this Commission takes on the role of the state in conducting mediation and arbitrations in accordance with Sections 251 and 252.

There are two main legal theories upon which the Commission could establish a rule that ISP-bound calls should be subject to the reciprocal compensation provisions of Section 251(b)(5). One is to re-think either (a) its earlier conclusion that Section 251(b)(5) should only be applied to "local" calls or (b) its statement in the *Declaratory Ruling* that ISP-bound calls are not local in nature. As to the limitation of Section 251(b)(5) to "local" traffic, nothing in the text of the law itself imposes any such limitation, which refers to compensation for "telecommunications." In this regard, the underlying purpose of limiting reciprocal compensation to "local" calls mainly related to the Commission's desire to avoid disrupting the access charge system. Since access charges do not apply to ISP-bound calls in any event, there is no policy reason — and, again, certainly no legal requirement — to exclude ISP-bound calls from reciprocal compensation obligations.[27]

As to the "local" nature of calls to ISPs — and putting aside the question of the severability of ISP-bound traffic into inter- and intrastate components — the Commission could conclude that while an overall "communication" from an end user to a distant Internet site is indeed interstate, the fact that an ISP's modem equipment is attached to a line with a local telephone number means that ***for purposes of Section 251(b)(5),*** calls to ISPs should be regarded as "local" in nature.[28]

The second way to reach this same result — bringing ISP-bound calls expressly within the reach of Section 251(b)(5) — is to extend, by analogy, the treatment of ISP-bound calls as exempt from access charges under Section 201 (and the treatment of ISPs as end users, not carriers, for purposes of Section 254 and Section 251) to the determination of the scope of

[27] There is plainly no basis for the assertions of some ILECs that only jurisdictionally intrastate traffic can be made subject to Section 251(b)(5). *See, e.g.* Southwestern Bell Comments at 5-6; Ameritech Comments at 15-20. Aside from the fact that nothing in the statute supports such a conclusion, that rule would have barred the Commission from determining that intra-MTA calls for broadband wireless traffic are subject to such compensation.

[28] This would no more constitute a repudiation of the rule that jurisdiction is determined on an end-to-end basis than the underlying ISP exemption from access charges does. To the contrary, it would simply be a recognition that as a matter of network engineering and call routing, ISP-bound traffic looks and feels like local calling, not toll calling.

reciprocal compensation obligations under Section 251(b)(5). Indeed, the Commission recognized in the *Declaratory Ruling* that the logical extension treating ISP-bound calls as though they were "local" in the access charge context would be to treat such calls as "local" for purposes of Section 251(b)(5) as well.[29]

In this regard, the access charge exemption — under which ISPs can purchase local exchange service to receive local calls from end users — has been sustained twice by the courts, once following its establishment in 1983, and once again following its reaffirmation in 1997.[30] There is no basis to suspect that the courts would find fault with a Commission conclusion that this same arrangement should apply to reciprocal compensation under Section 251(b)(5) — particularly in light of the Supreme Court's broad interpretation of the Commission's authority to adopt rules implementing the Act under Section 201(b).

It may be, however, that the Commission for some reason does not want to bring compensation for ISP-bound calls within the rubric of Section 251(b)(5). In that event, the Commission is free to establish rules regarding ISP-bound traffic on the basis of its authority, under Section 201, over all interstate traffic. It is hard to imagine an objection to the Commission's authority under this theory.[31] Under this approach the main question for the Commission is whether it wants ISP-bound traffic to be treated the same as local traffic for compensation purposes, or whether it wants to establish a regime under which carriers have to separately identify such traffic and handle it differently.

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[29] *See Notice* at ¶ 25 (this is a portion of the Declaratory Ruling, as opposed to the Notice of Proposed Rulemaking as such).

[30] *See NARUC v. FCC,* 737 F.2d 1095, 1135-1137 (D.C. Cir. 1984) (upholding initial "ESP Exemption"); *Southwestern Bell v. FCC,* 153 F.3d 523 8th Cir. 1998) (upholding permanent exemption for information service providers).

[31] The only conceivable objection would be that a significant portion of the traffic in question is really intrastate. While that may well be true (*see* Section 6, *infra*), that same conclusion would support reaching the economically correct result under the rubric of Section 251(b)(5).

To treat ISP-bound calls in the same manner as local, the Commission should state that, in an exercise of its authority under Section 201, it (a) will use compensation rates established through negotiation and/or arbitration as a reasonable proxy for the interstate costs LECs incur in delivering such calls to ISPs and (b) will direct any LEC originating such calls to another LEC to pay the relevant amount pursuant to the (new) federal rule.[32] To establish a separate regime for ISP-bound calls, the Commission should state that the compensation rate for ISP-bound traffic shall be some other figure, and direct LECs sending ISP-bound traffic to other LECs to pay that rate. (Global NAPs has suggested that the Commission use the ILEC's interstate local switching rate for this purpose). To allow for negotiations, the Commission could permit affected carriers to submit alternative compensation arrangements to the Commission in the form of an inter-carrier contract (which would be subject to Section 211 of the Act).[33]

Note in this regard that the fact that compensation is due for ISP-bound calls will have an extremely salutary effect upon the ILEC's charges for whatever service is used as the relevant proxy. The last several years have made painfully clear that CLECs are capable of targeting their marketing efforts to entities that receive calls. This has resulted in the ILECs having to ***pay*** CLECs for terminating calls. If the FCC chooses to link compensation level for ISP-bound calls to local reciprocal compensation rates (the practical situation today), then the

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[32] Note that under this legal option the Commission would not be directing the states to make any specific decisions regarding how any "interstate" traffic would be handled. The Commission would be establishing a ***federal*** rule that the ***Commission*** would rely on the results of state-level negotiations and arbitrations regarding local traffic to determine the correct ***interstate*** level for inter-carrier compensation for ISP-bound traffic. Particularly since the state-level negotiations and arbitrations will be taking place within the context of ***federally-mandated*** costing rules (the TELRIC standard), it would not be improper or irrational to rely on these state-level results.

[33] Global NAPs agrees that as a general matter the Commission may not simply delegate to state commissions the duty (or the authority) to set the rules for inter-carrier compensation for interstate traffic. It is clear, however, that ISP-bound traffic is a peculiar beast, which has been subject to special rules since the inception of the interstate access charge regime. That said, if the Commission wants to have state commissions handle arbitrations regarding ISP-bound traffic, Global NAPs believes that the Commission would be well-advised either to modify its "local only" interpretation of Section 251(b)(5) or to affirmatively rule (in an extension of the access charge exemption) that ISP-bound traffic should be treated as local for purposes of Section 251(b)(5) as well as for purposes of Section 201, so that the legal basis for state commission action — Section 252 — would be clear.

ILECs will have an extremely strong incentive to ensure that the reciprocal compensation rate is not set too high.

Over time, therefore, a policy of requiring compensation for ISP-bound calls will actually facilitate the development of competition for customers who make calls rather than receive them. This is because, as compensation rates are pressed lower and lower, excessive ILEC local usage charges will become subject to direct competitive pressure. If lower termination charges lead to a reciprocal compensation bill of only (say) \$0.005 for a "normal" 3-minute call, CLECs will find it ever more economically viable to compete for customers who originate traffic and have to pay message units (or flat-rated calling allowances) based on per-call costs that are 10 or 20 times that amount.[34]

On the other hand, if the compensation rate for ISP-bound traffic is pegged to the other logical (and, in light of the Commission's jurisdictional determination, probably more appropriate) benchmark — the ILEC's interstate local switching access charge rate element — that will put pressure on ILECs to lower interstate access charges towards cost, another important Commission goal. The fact that the ILEC actually has to ***pay*** that rate will produce a strong and healthy motivation for the ILEC to ensure that it is set at as low a level as is consistent with the ILEC's actual economic costs.

For these reasons, the Commission need not be concerned about the challenges to its authority to establish a compensation regime for ISP-bound traffic raised by various ILECs.[35] The Commission's decision will no doubt be taken to court, no matter what result is reached on the merits. But the danger of reversal is minimal. The Commission's authority over interstate traffic, and over the proper interpretation of Section 251(b)(5), is essentially plenary. As long as the substantive result reached is reasonable, and as long as the legal basis for the

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[34] As noted above, Ameritech's residence message unit in at least one of its states is \$0.05, and its business message unit is \$0.10.

[35] *See, e.g.,* Southwestern Bell Comments at 9-17; Ameritech Comments at 15-19.

Commission's action is clearly spelled out, ILEC bluster about what the Commission "must" or "must not" do in this area may safely be disregarded.

5. The Applicability of Section 252(i) Depends On The Commission's Legal Theory.

The *Notice* seeks comment on the applicability of Section 252(i) to agreements relating to the payment of compensation for ISP-bound traffic. *Notice* at ¶ 35. This is actually a simple question. The extent to which Section 252(i) applies follows directly from the legal theory on which the Commission chooses to base its decision in this case.

As discussed above, one legal option for the Commission is to direct that calls to ISPs be treated as subject to the reciprocal compensation obligation of Section 251(b)(5). If the Commission takes that course, then the provisions of Section 252(i) will apply to interconnection agreements that embody that obligation, including as it applies to ISP-bound calls. If the Commission instead acts under its general Section 201 authority regarding interstate traffic, then Section 252(i) would not apply. Instead, the general obligation of interstate carriers to be just, reasonable and non-discriminatory would control the extent to which an agreement between an ILEC and CLEC "A" would also be available to CLEC "B."[36]

From Global NAPs' perspective, the significance of Section 252(i) to this issue has been greatly inflated by the ILECs' own intransigence on the underlying question of whether ISP-bound calls are subject to compensation at all. Prior to the issuance of the *Declaratory Ruling* (and, indeed, after it) essentially every state to consider the question concluded that ISP-

[36] Various ILECs have used their comments in this matter to argue that the provisions of Section 252(i) do not apply to reciprocal compensation arrangements in any event. *See, e.g.,* Ameritech Comments at 21-26. The Commission should disregard these comments because they are well beyond the scope of this proceeding (and essentially amount to a collateral attack on the Commission's newly-reinstated rules regarding Section 252(i)). To the extent that the Commission considers them, however, they are wrong. Under Section 252(i) and the Commission's implementing regulation (47 U.S.C. § 51.809), interconnection must be made available to any CLEC on the same "terms and conditions" as included in any state-approved ILEC interconnection agreement with any other CLEC. It is ludicrous to assert that when and whether a CLEC pays or gets paid for traffic exchanged by means of an interconnection arrangement is not a "term" or "condition" of that interconnection.

bound calls were subject to reciprocal compensation in the same manner as local calls.[37] This overwhelming unanimity among state commissions notwithstanding, ILECs routinely asserted that they would not sign any new interconnection agreement that provided for such compensation. This meant that established CLECs (such as MFS, TCG and others) could serve ISPs and receive compensation (or at least accrue reasonably solid "receivables") based on their original agreements. Newcomers, however, would not be able to compete for such business, because the ILECs would not enter into a contract that provided for such compensation.[38] The only practical way to enter the market on the same terms on which existing CLECs were already operating was to opt into an existing agreement.[39]

In this regard, the entire notion that CLECs can unreasonably and unfairly "daisy chain" an agreement is a complete red herring. Suppose that some misguided ILEC has signed an agreement with a five-year term and a per-minute compensation rate equal to its intrastate access charges (on the theory that such charges represent a reasonable estimate of the cost of handling calls in that jurisdiction). Suppose further that the ILEC is now being hammered by CLECs who have rushed to sign up ISPs, take-out pizza parlors, taxicab dispatch services, voice mail services, fax forwarding services, etc., in order to exploit the ILEC's poor business

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[37] *See* Comments of Focal Communications, Inc. at 2 n.6 for what appears to be a full listing of the relevant state decisions.

[38] In practical terms, ILECs started including a "non-negotiable" provision in their "standard" interconnection agreements that specifically excluded ISP-bound calls from reciprocal compensation. Even if a CLEC had some basis to believe (*e.g.*, based on an earlier state commission decision) that the state commission would uphold the compensation obligation in arbitration, the price of obtaining the same reciprocal compensation terms as the established CLECs was a delay of 9 months or more in entering the market.

[39] Beginning no later than August 1998, Bell Atlantic ceased allowing Global NAPs at least, and perhaps other CLECs as well, from opting in to existing agreements. Bell Atlantic implemented this anticompetitive strategy by refusing to allow Global NAPs to opt into the "same" agreement that Bell Atlantic had with other CLECs, unless Global NAPs would sign a document agreeing to Bell Atlantic's particular interpretation of that agreement — including, specifically, agreeing that ISP-bound traffic was not subject to compensation. Global NAPs, therefore, has had to arbitrate its disputes with Bell Atlantic even though all Global NAPs wanted was ***the same deal that Bell Atlantic had already given to other CLECs.***

judgment. Is the ILEC stuck with its bad deal? That depends entirely on the relevant state commission.

Any time a CLEC "opts into" the (from the ILEC's perspective) ill-considered agreement under Section 252(i), that creates an agreement between the ILEC and the new CLEC that must be submitted to the state commission for approval pursuant to Section 252(e). Assuming that the opted-into agreement is treated as having been "adopted by negotiation," the ILEC is free to argue under Section 252(e)(2)(A) that the terms it doesn't like (in this hypothetical, the reciprocal compensation rate and the five-year term) are discriminatory under Section 252(e)(2)(A)(i), or not in the public interest under Section 252(e)(2)(A)(ii). If the state commission agrees, then the agreement cannot be "daisy chained." Conversely, the only way an agreement ***can*** be "daisy chained" is ***if the state commission finds it to be non-discriminatory and in the public interest.*** It is hard to see what cognizable "harm" befalls the ILEC when the state commission concludes that the agreement is non-discriminatory and in the public interest.[40]

Moreover, the Supreme Court's reinstatement of this Commission's "pick and choose" rule provides significant guidance to ILECs, CLECs, and state commissions regarding whether particular provisions in an "opted into" interconnection agreement are, in fact, properly available to the CLEC seeking to take advantage of them. That rule gives the ILECs ample opportunity to prevent the "daisy chaining" of terms in agreements that should not be made available beyond the duration of a particular agreement.[41]

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[40] The same logic would apply if the agreement is treated as arbitrated and, therefore, subject to review under Section 252(e)(2)(B). If the provisions that the ILEC doesn't like (again, the reciprocal compensation rate and the five-year) are inconsistent with Section 251 and Section 252(d), then the state commission will disapprove the agreement. If those provisions ***are*** consistent with Sections 251 and 252(d), then it is again hard to see what real objection the ILEC has.

[41] In this regard, Global NAPs admits to being the CLEC referred to in the *Notice* that obtained an arbitration decision that awarded a three-year agreement that included relatively high reciprocal compensation rates, including ISP-bound traffic. Bell Atlantic apparently presented this decision as some sort of outrage for the Commission's shocked and horrified consideration. In fact the situation was much more mundane. Bell Atlantic entered into a contract with MFS that included a variety of rights and duties for both parties. In any number of cases, the performance of the duties and/or the (continued...)

In any case, this entire problem should disappear once the Commission issues its ruling in this proceeding. The ILECs are firmly committed to the idea that ISP-bound calls are jurisdictionally interstate, which means that they cannot credibly contest this Commission's authority to set the rules that apply to such calls. This may be wishful thinking on Global NAPs' part, but in light of ILEC statements regarding the Commission's authority, it is probably reasonable to assume that the ILECs will comply with whatever rules the Commission establishes for inter-carrier compensation for ISP-bound calls. If the Commission chooses to adopt a legal rationale that subjects ISP-bound traffic to Section 251(b)(5), then it seems reasonable to assume that the ILECs will comply with the Commission's order. If they do so, while some CLECs may or may not choose to avail themselves of their Section 252(i) rights, they will not be compelled to rely on these rights simply to obtain equal treatment with other, established CLECs on this particular issue.

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[41](...continued)
exercise of the rights was expressly "staged" over a period of months or even, in some cases, years. The ***substantive provisions of the contract,*** in other words, clearly envisioned a contract term of several years. Moreover, the state commission (the New Jersey BPU) had clearly understood the original contract as involving performance by both parties over an extended period of time. This was shown by the fact that the order approving the original contract referred to it as having a "three year" term. In the arbitration in question, Global NAPs argued (based on the express language of the contract, the express language of the state commission order approving it, and an analysis of the contract's substantive terms) that it was entitled to the stability offered by a three-year contract that included the same substantive terms as contained in the MFS agreement into which Global NAPs was seeking to "opt in." The arbitrator agreed with Global NAPs as a matter of contract interpretation.

The Commission need not be unduly troubled that Bell Atlantic has been subject to some sort of injustice by this decision. While one can always second-guess any adjudicatory decision regarding the meaning of a complex contract, Bell Atlantic has steadfastly refused to honor or implement the arbitrator's decision, and the New Jersey BPU has refused either to accept the arbitrator's decision or to enter a decision modifying it. The result is that more than a year after Global NAPs initiated negotiations with Bell Atlantic in New Jersey, Global NAPs has ***no interconnection agreement with Bell Atlantic at all*** in that state. Global NAPs will shortly be filing a petition with this Commission to assume the duties of the New Jersey Board in this matter, given that body's inability or unwillingness to fulfill its obligation to determine the terms of an interconnection agreement between an ILEC and a CLEC who cannot agree.

6. ISP-Bound Traffic Is Reasonably Severable And Largely Intrastate.

The ILECs take some pains to try to prop up the Commission's tentative conclusion in the *Notice* that ISP-bound traffic is not severable into interstate and intrastate components.[42] Both they and, with due respect, the Commission, are wrong.[43]

When a customer's modem calls an ISP's modem, these two devices immediately establish a complex and highly structured set of signals between them. These signals are used to keep the two devices "in synch" with each other; in effect, they form a low-level signal framework within which high-level data may be transmitted at the fastest rate possible given the capacities of the modems themselves and the capabilities of the circuit-switched connection between them.

Whatever may be said about how hard it is to sort out the jurisdictional status of signals sent from the customer to a distant web site and back, there is no ambiguity whatsoever about the modem synchronization signaling just described. It starts at the end user's premises and ends at the ISP's modem. Period. This signaling is "local" in exactly the same way, and to exactly the same extent, that calls from an end user to the ISP's local sales office or technical support personnel are "local."

Moreover, during a dial-up session, these modem synchronization signals constitute that vast majority of the traffic actually exchanged between an ISP and an end user. This occurs for two simple reasons. First, once an end user has downloaded data (*e.g.*, from a web site or email server), it takes the user some time to review it. Depending on the type of file downloaded, the ratio between the time it takes to download (when higher-level data might be

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[42] *See, e.g., Notice* at ¶ 38; Bell Atlantic Comments at 7-8; US West Comments at 18-19; Ameritech Comments at 27-29; BellSouth Comments at 10-12.

[43] This section expands upon the brief discussion of this point included in Global NAPs' initial comments. *See* Global NAPs Comments at 9 n.19.

coming from a distant site) and the time it takes to review it (when the only signaling is between the modems) can be very small indeed.

Second, once an end user has established a connection to an ISP, it is not totally unheard of for the connection to remain active while the end user attends to other matters, such as ordering (and perhaps eating) a pizza, answering a telephone call, etc. The flat-rated ISP usage plans that the market has demanded obviously do not encourage end users to disconnect when they are not actively using a connection. For precisely this reason, many ISPs have implemented procedures that automatically disconnect end users when there has been no higher-level data exchanged for a sufficiently long period of time. These expenditures would not be needed if end users were careful about maximizing the actual amount of data that they download per minute of time spent on line.

Objective evidence supports the conclusion that the vast majority of traffic between end users and ISPs is local modem synchronization signals. ISPs generally apply a 10:1 concentration ratio for the bandwidth coming into their modem banks and the bandwidth connecting those modem banks to the ISP's routers and servers.[44] This means that at any given moment, out of any ten customers logged in to the ISP, only one is actually sending or receiving higher-level data calling for involvement by the ISP's routers or servers.

Recognizing that the vast majority of actual traffic exchanged between end users and ISPs is local in nature is not an effort to revive the "two call" theory through the back door. The Commission's own analysis of the jurisdictional question proceeds from the assumption that the exchange of data between an end user and an in-state location on the Internet is an "intrastate" communication, while a similar exchange of data between an end user and an out-of-state location is an "interstate" communication.[45] The realities of dial-up traffic described above,

[44] *See* Statement of Fred Goldstein, attached to Comments of Global NAPs.

[45] One can imagine theories of federal jurisdiction over dial-up calls to ISPs that do not depend upon the specific traffic patterns discussed here. For example, one could imagine treating the entire
(continued...)

although not addressed in the *Declaratory Ruling* or the *Notice*, make it certain that the vast majority of the actual traffic exchanged over dial-up connections is intrastate and local, even if the packets that travel to and from distant Internet sites are entirely interstate in nature.[46]

The fact that it is not possible to obtain accurate, real-time measurements of which traffic falls into which category is no obstacle to imposing a general rule that ISP-bound traffic shall be presumed to be (for example) 90% local and 10% interstate. In this regard, the ILECs themselves are quick to draw analogies between the ISPs' dial-up lines and traditional Feature Group A lines used to provide interstate access services in pre-equal-access times.[47] The Commission will recall, however, that when Feature Group A lines were used to offer both inter- and intra-state long distance services, the affected carriers were able to develop "percent interstate use" or "PIU" factors to determine the appropriate billing of inter- and intrastate Feature Group A access rates. Exactly the same approach can and should be used in the case of dial-up calls to ISPs.[48]

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[45](...continued)
Internet as, in effect, an interstate private network, and treat the ISPs' facilities — including their modems — as the "final outposts" of this network. Under this theory, a call to any ISP anywhere would be jurisdictionally interstate, no matter how much traffic goes where once it reaches the ISP. But this is not the theory the Commission has adopted.

[46] The proportion of traffic that could properly be classified as local is even higher for ISPs that make extensive use of caching techniques. With a well-managed cache, a substantial fraction of web sites that a user may think are coming from a distant location are, in fact, coming from the ISP's own facilities.

[47] *See, e.g.,* US West Comments at 4.

[48] Global NAPs believes that a reasonable first approximation of the relevant jurisdictional split is roughly 93% intrastate/local, and roughly 7% interstate. This is based on an assumption that 90% of the traffic is local modem synchronization signaling, and that 30% of the actual higher-level data end users obtain is either intrastate or (more likely) resident in an ISP cache. These figures could be subject to periodic updating based on information obtained from ISPs, carrier-to-carrier negotiation, or other sources.

7. Conclusion.

Requiring compensation from an originating LEC, who delivers traffic to a LEC, who forwards it on to an ISP, is economically rational and pro-competitive. Overall economic efficiency is served as long as the rate of compensation is roughly equal to the costs that the originating LEC (typically the ILEC) would incur to perform those terminating switching functions on its own. The Commission, moreover, has ample legal authority to order the establishment of such a compensation requirement, under either Section 201(a) (applicable to interstate traffic in general) or Section 251(b)(5) (on the same logic as the ISP access charge exemption, twice sustained by the courts).

In any case, however, it is clear as a technical matter that the vast majority of traffic between end users and ISPs transmitted over dial-up connections is purely local, because it never actually goes any further into "the Internet" than the ISP's modems. The Commission, therefore, should establish a presumption that 90% or more of ISP-bound traffic is local traffic, subject to normal reciprocal compensation obligations under Section 251(b)(5).

Respectfully submitted,

GLOBAL NAPS, INC.

By: ______________________

Christopher W. Savage
Karlyn D. Stanley
COLE, RAYWID & BRAVERMAN, L.L.P.
1919 Pennsylvania Avenue, N.W., Suite 200
Washington, D.C. 20006
202-659-9750

William J. Rooney, Jr
General Counsel, Global NAPs Inc.
Ten Merrymount Road
Quincy, MA 02169
617-507-5111

Date: April 27, 1999

CERTIFICATE OF SERVICE

I, Linda M. Blair, hereby certify that on this 27th day of April, 1999, I caused a copy of the foregoing, Reply Comments of Global NAPs Inc. to be sent via messenger (*) or by, postage paid to the following:

*Ms. Magalie Roman Salas
Secretary
Office of the Secretary
Federal Communications Commission
445 12th Street, SW - Room TW-A325
Washington, DC 20554

*Wanda Harris (w/ diskette)
Competitive Pricing Division
ommon Carrier Bureau
Federal Communications Commission
445 12 Street, SW - 5th Floor
Washington, DC 20554

Gail J. Polivy
GTE Service Corporation
1850 M Street, NW Suite 1200
Washington, DC 20036

Leon M. Kastenbaum
Jay C. Keithly
Sprint Corporation
H. Richard Juhnke
1850 M Street, NW 11th Floor
Washington, DC 20036

Angela D. Ledford, Executive Director
Keep America Connected
P.O. Box 27911
Washington, DC 20005

Gary Phillips, Esq.
Ameritech
1401 H Street, NW
Suite 1020
Washington, DC 20005

Willkie Farr & Gallagher
Counsel for Time Warner Telecom
3 Lafayette Center
1155 21st Street, NW
Washington, DC 20036

George Vradenburg, III
Jill A. Lesser
Steven N. Teplitz
America Online, Inc.
1101 Connecticut Avenue, N.W.
Suite 400
Washington, D.C. 20036

Donna N. Lampert
Donna M. Lampert & Associates, P.C.
701 Pennsylvania Avenue, NW
Suite 200
Washington, DC 20004

Richard M. Rindler
Patrick J. Donovan
Swidler Berlin Shereff Friedman, LLP
3000 K Street
Suite 300
Washington, DC 20007

Richard Metzger
Focal Communications Corporation
1120 Vermont Ave., NW
Terrace level
Washington, DC 20005

Randall B. Lowe
Counsel for Prism Communications Services Inc.
Piper & Marbury
1200 Nineteenth Street, NW
Washington, DC 20036

Robert M. Lynch
Roger K. Toppins
Michael J. Zpevak
Kathleen E. Palter
SBC Communications Inc.
One Bell Plaza, Rm. 3014
Dallas, TX 75202

Cindy Z. Schonhaut
ICG Communications, Inc.
161 Inverness Drive W., 6th floor
Englewood, CO 80112

Albert H. Kramer
Robert F. Aldrich
Dickstein Shapiro Morin & Oshinsky, LLP
2101 L Street, NW
Washington, DC 20037
Kenneth T. Burchett
Vice president
GVNW Consulting, Inc.
8050 S.W. Warm Springs St.
Tualatin, Oregon 97062

David Ellen
Senior Counsel
Cablevision Lightpath, Inc.
1111 Stewart Avenue
Bethpage, NY 11714

Cheri R. Kiser
Gil M. Strobel
Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C.
701 Pennsylvania Avenue, NW Suite 900
Washington, DC 20004

Caressa D. Bennet
CT Cube Inc and LEACO Rural Telephone Cooperative, Inc.
Bennet & Bennet, PLLC
1019 Nineteenth Street, NW Suite 500
Washington, DC 20036

George N. Barclay
Michael J. Ettner
General Services Administration
1800 F Street, NW Rm. 4002
Washington, DC 20405

Carl W. Northrop
AirtouchPaul Hastings Janofsky & Walker LLP
1299 Pennsylvania Avenue, NW
Washington, DC 20004

Charles C. Hunter
Catherine M. Hannan
Hunter Communications Law Group
1620 I Street, NW Suite 701
Washington, DC 20006

Douglas Denny-Brown
RNK Inc.
1044 Central Street
Stroughton, MA 02072

Cheryl A Tritt
Charles H. Kennedy
Morrison & Foerster LLP
2000 Pennsylvania Avenue, NW
Washington, D.C. 20006

Lorinda Ackley-Mazur
Executive V.P.
Richmond Telephone Company
1416 State Road
Richmond, MA 01254

Richard S. Witt
MCI WorldCom, Inc.
1801 Pennsylvania Avenue, NW
Washington, DC 20006

M. Robert Sutherland
Richard M. Sbaratta
BellSouth Corporation
Suite 1700
1155 Peachtree Street, NE
Atlanta, GA 30309

Emily M. Williams
ALTS, Suite 900
888 17th Street, NW
Washington, DC 20006

William Page Montgomery
Montgomery Consulting
2903 Alta Laguna Blvd.
Laguna Beach, CA 92651

Charles H. Eppert III
Bell Atlantic Corporation
1310 N. Courthouse Road
Arlington, VA 22201

David Cosson
Kraskin, Lesse & Cosson, LLP
2120 L Street, NW, Suite 520
Washington, DC 20037

Samuel E. Ebbeson
President & Chief Executive Officer
Virgin Islands Telephone Company
P.O. Box 6100
St. Thomas, USVI 00801-6100

Gerald W. Brock
On behalf of Cox Communications Inc.
Professor of Telecommunication
The George Washington University
812 20th Street, NW
Washington, DC 20052

Michael J. Shortley, III
Frontier Communications
180 South Clinton Avenue
Rochester, NY 14646

Kathy L. Shobert
Director
General Communication Inc.
901 15th Street, NW
Suite 900
Washington, DC 20005

Mark C. Rosenblaum
Stephen C. Garavito
AT&T Corp.
Room 325G1
295 North maple Avenue
Basking Ridge, NJ 07920

David L. Lawson, James P. Young,
Daniel Meron, Rudolph M. Kammerer
Sidley & Austin
1722 Eye Street, NW
Washington, DC 20006

Jonathon J. Nadler
Brian J. McHugh
Squire, Sanders & Dempsey, LLP
1201 Pennsylvania Avenue, NW
Washington, DC 20044

Ronald L. Plesser
Mark J. O'Connor
Piper & Marbury
1200 Nineteenth Street, NW
Suite 700
Washington, DC 20036

Robert J. Aamoth, Steven A. Augustino
John J. Heitmann
Kelley Drye & Warren, LLP
1200 19th Street, NW
Fifth Floor
Washington, DC 20036

Jonathon E. Canis
Ross A. Buntrock
Kelley Drye & Warren, LLP
1200 19th Street, NW
Fifth Floor
Washington, DC 20036

Terry Monroe
VP, State Affairs
COMPEL
1900 M Street, NW
Suite 800
Washington, DC 20036

Carol Ann Bischoff
Executive VP
COMPEL
1900 M Street, NW
Suite 800
Washington, DC 20036

Robert L. Hoggarth, Esq.
Angela E. Giancarlo, Esq.
Personal Communications Industry
Association
500 Montgomery Street, Suite 700
Alexandria, VA 22314

William T. Lake, John H. Harwood II
Lynn R. Charytan, Jonathon J. Frankel
Wilmer Cutler & Pickering
2445 M Street, NW
Washington, DC 20037

Robert B. McKenna
Jeffrey A. Brueggeman
US West Inc.
1020 19th Street, NW
Washington, DC 20036

Cynthia B. Miller, Esq.
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, FL 32399

Jan F. Reimers
President
ICORE, Inc.
326 S. Second Street
Emmaus, PA 18049

Nancy A. Russell
State of New York Dept. of Public Service
3 Empire State plaza
Albany, NY 12223

Sandy Ibaugh
Indiana Utility Regulatory Commission
302 W. Washington Street, Room E306
Indianapolis, Indiana 46204

Steve Davis
Director, Office of Policy Development
Public Utility Commission of Texas
1701 N. Congress Ave.
P.O. Box 13326
Austin, TX 78711

Eric J. Branfman
Swidler Berlin Shereff Friedman, LLP
3000 K Street, NW, Suite 300
Washington, DC 20007

Barry Pineles
GST Telecom Inc.
4001 Main Street
Vancouver, WA 98663

Dana Frix
Pamela S. Arluk
Swidler Berlin Shereff Friedman LLP
3000 K Street, NW Suite 300
Washington, DC 20007

Joseph Kahl
RCN Telecom Services, inc.
105 Carnegie Center
Princeton, NJ 08540

Ray J. Riordan, Jr.
Executive VP
Wisconsin State Telecommunications
Association
6602 Normandy Lane
Madison, WI 53719

*ITS - 1231 20th Street, NW
Washington, DC 20036

Peter Arth Jr.
Lionel B. Wilson
Ellen S. Levin
People of the State of California and the
CA PUC
505 Van Ness Avenue
San Francisco, CA 94102

Christopher J. Wilson
Cincinnati Bell Telephone Company
201 East 4th Street, Room 102-620
Cincinnati, OH 45201

Susan M. Eid
Richard A. Karre
MediaOne Group - Suite 610
1919 Pennsylvania Avenue, NW
Washington, DC 20006

L. Marie Guillory
Jill Canfield
National Telephone Cooperative
Association
2626 Pennsylvania Avenue, NW
Washington, DC 20037

Thomas R. Parker
John F. Raposa
GTE Service Corporation
600 Hidden Ridge
HQE03J27
Irving, Texas 75038

Douglas M. Meredith
John Staurulakis, Inc.
6315 Seabrook rd.
Seabrook, MD 20706

Peter Bluhm, Esq.
Vermont Public Service Board
112 State Street, Drawer 20
Montpelier, VT 05620-2701

Linda M. Blair

Linda M. Blair